Cashability

Discussion paper

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CONTENTS

1 Purpose

1.1 This paper was initially produced in response to requests from personnel involved in public service reform (PSR) across Greater Manchester (GM). It is, however, relevant for any public service reform programmes across the UK. It considers issues around 'cashability' – how anticipated savings from PSR interventions can be 'taken out of the system' through targeted decommissioning. In particular, the paper seeks to inform conversations between partners on cost benefit analysis (CBA) and the implications of CBA findings for discussions around decommissioning and financial planning.

1.2 The paper covers the following areas:

- defining what we mean by cashability, and articulating the distinction between cashable savings and general benefits
- considering factors that impact upon cashability, and ways in which resources might be made more cashable
- understanding the strategic implications for PSR activity
- providing examples of cashability assumptions, used as a starting point for PSR modelling.

2 Definition

Cashability refers to the extent to which a change in an outcome or output (e.g. fewer children in care)or an improvement in the way these outcomes are achieved (e.g. process efficiencies) will result in a reduction in fiscal expenditure such that the expenditure released from that change can be reallocated elsewhere.

2.1 Key points that follow are:

- a cashable saving is distinct from a fiscal benefit; some benefits are more straightforward to cash than others
- cashability varies according to organisational strategy, cost type and scale; cashability can increase through reform
- ultimately all savings are cashable if budgets are cut
- effective PSR requires an understanding of the different levels of cashability of benefits that fall to different organisations, both under the 'as is' situation, and if reforms were made to enhance cashability
- cashable benefits can be re-used in different ways; PSR involves some reinvestment of cashable benefits.

2.2 Different types of costs have different cashability characteristics:

- **fixed costs** do not vary significantly with scale. If demand is reduced, the fixed costs of a delivery model will stay relatively similar. Fixed costs are generally more difficult to cash at a lower scale of operation. However, fixed costs also tend to be non-linear, and may be extremely cashable at a specific threshold scale. For example, the minimum unit of cashability for health providers is generally considered to be a hospital ward
- **variable costs** are closely linked to the scale of production. Variable costs can be more easily cashed at all scales of reduced demand. The relationship between cashability and scale tends to be linear.

3 Practical issues involved in cashing a benefit

3.1 **Cashability will be influenced by the strategic financial approaches of individual organisations**, including their resource management and planning, approaches to risk and their cost base. Organisations will tend to balance cashability considerations against affordability and quality when making individual decisions, for example whether to procure on a spot purchase or block contract basis.

3.2 **Cashing benefits takes time**. There may be cultural barriers to realising cashable savings, particularly among organisations that have grown used to regular increases in budgets and finding ways to meet demand pressures. Commissioners will require a level of confidence before making a decision to decommission existing services that are no longer needed. This will mean sustaining a reduction in demand over a period of time, evidencing that levels of demand have reduced to a new business as usual level rather than a temporary reduction. Decommissioning decisions will tend to take account of wider resource management issues across other business areas, and it may be difficult to link causally the impact of specific interventions to reductions in demand.

3.3 **Cashing a saving will often incur an additional cost,** particularly if there is a change to an agreed contract. For example, significant staffing reductions beyond natural wastage may have redundancy implications. As a further example, preparing a property for sale on the market (therefore realising a capital receipt as well as reduced revenue running costs) will generally require up-front expenditure.

3.4 **Potential cashable savings may be offset by backfilling.** Organisations may decide to fill the capacity generated by a reduction in demand by an increase in demand from other cohorts of people, or a supply-side led drive to open up services to additional cohorts. In such cases it can be difficult to separate the original impact of the demand reduction from the subsequent change that led to the backfilling. For example: courts may sentence more people to custody if the stock prison population reduces; hospitals have incentives to fill beds that are no longer required for acute patients with complex tertiary operations that attract higher tariff payments. It may be possible to limit backfilling in some systems by maintaining thresholds of need within assessment systems, for example consistent assessments and criteria for local authority social service interventions.

3.5 **Cashability is more likely to be prioritised where the monetary value associated with an outcome is significant.** If the monetary value of the outcome is relatively small, decommissioning of business as usual is unlikely to be a key priority.

4 Making resources more cashable

4.1 Organisations can decide to increase the level of cashability through a range of options, which will be weighed against cost and quality implications:

- **commissioning and procurement** – moving to more flexible contracting arrangements, for example, moving from a block contract to a spot purchase or call-off arrangement, organising contracts over shorter time periods, and/or chunking larger contracts into smaller individual elements
- **workforce reform** – facilitating the movement of in-house staff across internal or external organisational boundaries, which may be supported by additional training and/or multi-disciplinary team structures
- **property management –** to help reduce the fixed costs related to property, and/or to realise a capital receipt on owned property, options include inserting more flexible break clauses into leases and contracts and renegotiating existing leases and contracts. Variable costs can be reduced and cashed by improving space utilisation and increasing energy efficiency.

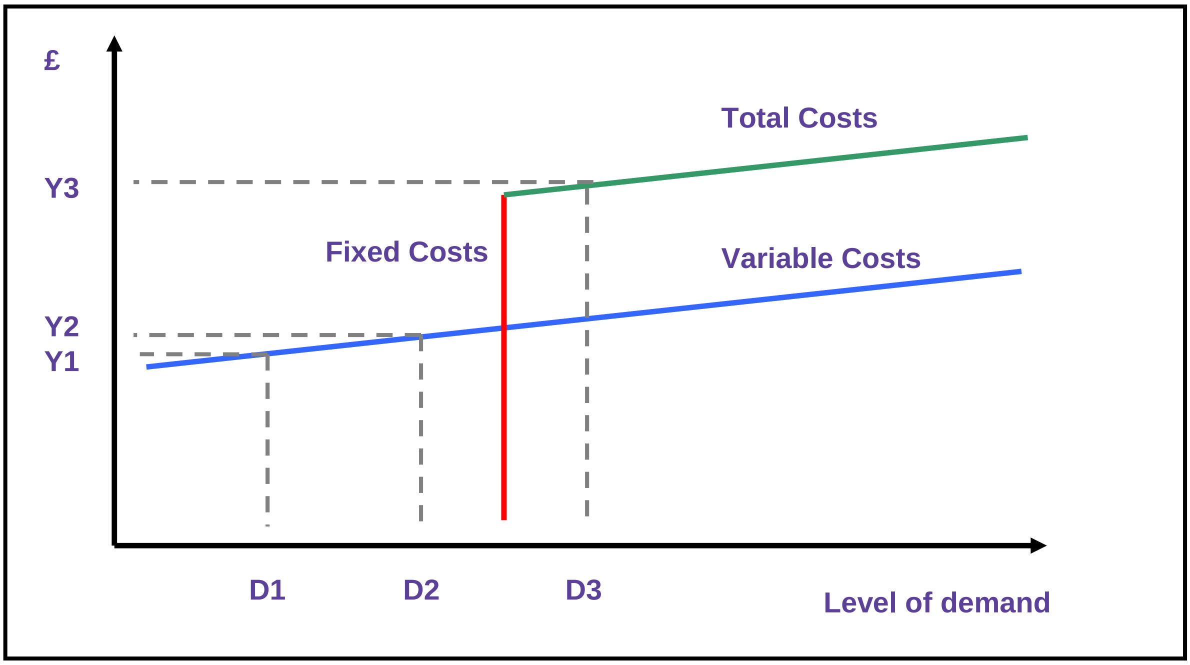
5 Strategic implications for public service reform

5.1 **Who cashes the benefit?** PSR investment models aim to move flexible resources across organisational boundaries for investment in cross-cutting delivery models that will improve outcomes and generate savings. Benefits can only be cashed at the level those resources are controlled. Many local organisations can make local decisions to cash savings and can therefore have more confidence investing in delivery models that should reduce demand – such as the police, schools, local authorities and health commissioners. Financial restrictions and externally imposed performance regimes will impact on those local decisions. For those resources controlled at higher spatial levels, such as prison funding which is managed nationally, negotiations about what and when to cash will be within the context of broader resource management strategies.

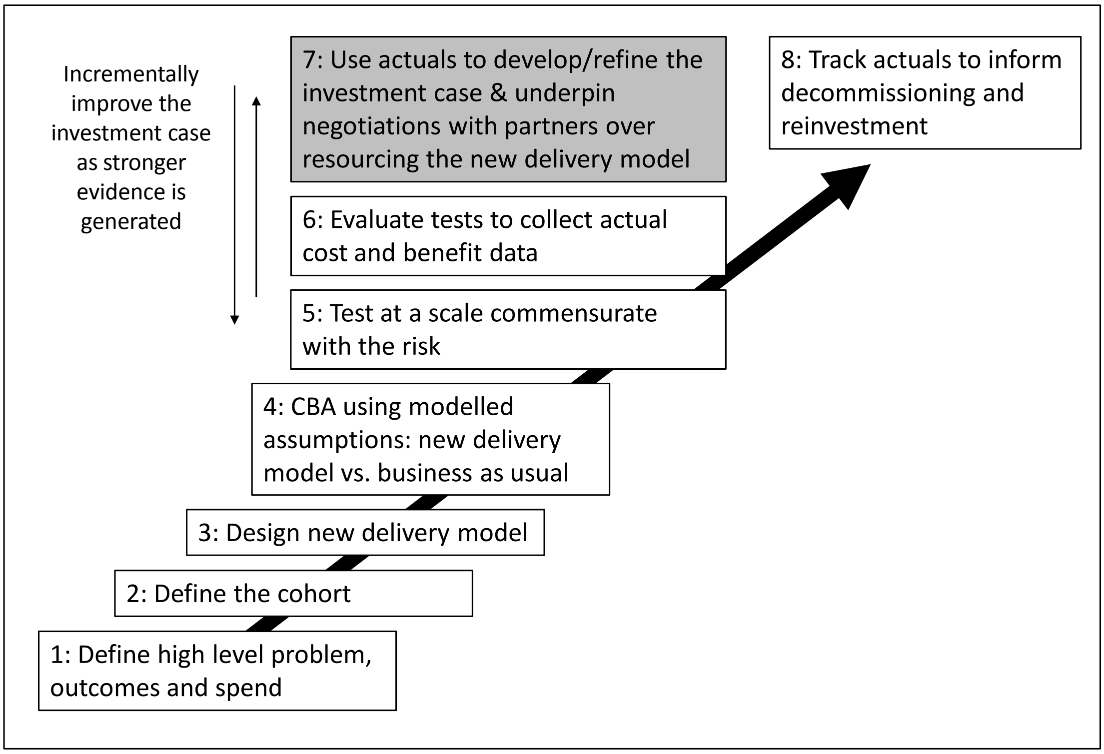
5.2 **Ultimately all benefits can be cashed by government.** Where national organisations decide not to cash a benefit related to a local reduction in demand (for whatever reason), government can ultimately decide to reduce that organisation's settlement to generate a cashable benefit, and force local decisions on how to cash.

5.3 **When will the benefit be cashed?** As outlined above, commissioners will have more confidence to decommission existing services that are no longer needed if reductions in demand are sustained over time. PSR interventions will therefore have greater impact if time-limited interventions have an ongoing impact on demand and dependency, and if ongoing interventions are implemented where required to hard-wire impacts into individual behaviours (for example, being in a sustainable job rather than moving in and out of low-pay, low-skill, insecure employment).

5.4 **Cashability increases with scale**, particularly in terms of being able to cash fixed costs as well as variable costs. There may be thresholds above which reduced demand becomes significant. The chart below shows how reducing demand from D3 to D2 realises a significant saving (Y3 to Y2) as fixed costs fall as well as variable costs, whereas a similar demand reduction from D2 to D1 realises very few savings (Y2 to Y1) just from the variable cost element. Scaling up PSR interventions will tend to realise proportionately more cashable savings than running a series of small-scale projects with a limited impact on demand.



5.5 **Utilising the cashable saving.** The GM PSR investment methodology illustrated below assumes that a proportion of cashable savings will be reinvested in PSR interventions, to help scale up existing activity and/or support new propositions focused on early intervention and prevention.



5.6 In addition to reinvestment in reform activity, cashable savings can also be used in a range of other ways including:

- **helping to meet existing savings targets or budget reductions**, particularly if these targets may not be delivered by existing interventions. If cashable savings realised by PSR interventions are used to help meet existing targets (e.g. health QIPP targets), particularly where these may not otherwise be delivered, this impact should be properly documented in order to help measure PSR impact
- **soaking up latent demand**, where new delivery models help to uncover previously unknown demand as more individuals and families come forward with needs that could be met effectively through these interventions. Again, this should be properly documented to measure the impact of PSR interventions
- **reinvestment in other priorities** either by the individual organisations receiving the benefit, a partnership, or by budget-setting organisations including government departments and national agencies.

5.7 In reality, cashable savings may well be shared between several of these uses. The GM CBA model enables PSR impact to be quantified, highlighting holistic fiscal, economic and social benefits. It also provides an initial starting point to consider cashability, by calculating two metrics:

- an initial estimate of the proportion of fiscal savings that may be cashable in the short-term
- an estimate of the proportion that may be cashable in the medium to longer term (i.e. in the final years of the modelling period), once interventions and outcome achievement have reached a certain scale. Definitions of short, medium and longer-term will depend on the chosen modelling period (i.e. the number of years over which benefits are profiled).

5.8 Organisations should consider what they can do to increase cashability, by adopting a more flexible organisational focus, and using some of the techniques outlined above. Ultimately, partners in investment negotiations have discretion over how they propose to cash required savings, either from cash, in kind, or both.

5.9 Effective leadership is also an important factor. A strong commitment to drive PSR forward, and take what may be difficult decisions in decommissioning business as usual, can increase the extent to which cashable savings are achieved. However, if several agencies are involved in delivering an intervention that leads to successful outcomes and resulting benefit, it may be difficult to achieve consensus across these agencies around which elements of business as usual should be decommissioned. Furthermore, it may be politically controversial to decommission certain areas of service provision (e.g. hospital accident and emergency services); in such cases, persuasive leadership and communication is of particular importance.

5.10 Robust monitoring processes need to be in place to ensure that savings are being cashed as anticipated. Evaluation methodologies should capture the impact of PSR interventions in reduced demand for reactive provision, the extent to which this demand reduction is reflected in the decommissioning of existing services, and how the cashable savings that are realised are subsequently used.

6 Examples of cashability assumptions

6.1 It is not possible to predict levels of cashability accurately, and even the best estimations will be approximate. The percentages outlined in the table below are used in the latest version of the GM CBA model (4.2)[1] to provide an indication of the extent to which estimated fiscal savings may be cashable, and to highlight potential differences across partners and over time. These figures are based on local discussions with partners in Greater Manchester and from experience of the cashability approach applied for national PbR programmes that GM have been involved with such as the MoJ Financial Incentive Mechanism. CBA findings derived from these metrics provide an initial starting point, following which detailed discussion over cashability and associated decommissioning will need to take place with commissioners and providers. CBA, therefore, informs discussions around how far benefits are cashable, but is not a substitute for negotiation.

Beneficiary agency	Short term / small scale cashability	Long term / large scale cashability	Rationale
Local authority	50%	90%	Many of the large cost savings relate to spot purchased services (e.g. residential care for Looked after Children), and are therefore relatively cashable. However, not all of this will be cashable in the short term due to the timing of contract renewals.
NHS	20%	50%	In the short term, savings relate to the marginal costs of prescribing drugs and providing treatment. A larger scale is required to enable significant changes such as ward closures. However, there will still be significant levels of fixed costs.
Police	30%	60%	Savings relate to reduction in staff with reduced demand. However, not all of this will be cashable due to the need to cater for one off events (e.g. riots). Due to the restrictions on making police officers redundant, these will also take time to realise.
Probation	20%	50%	Based on MoJ assumption of short term cashability. Fixed costs assumed to limit the scope of cashability in longer term.

[1] Available at http://neweconomymanchester.com/stories/1855-cost_benefit_analysis_guidance_and_model

Beneficiary agency	Short term / small scale cashability	Long term / large scale cashability	Rationale
Courts / Legal Aid / Prisons / Other criminal justice system	20%	50%	Based on MoJ assumption of short term cashability. Significant fixed costs such as the prison estate limit cashability in the longer term.
DWP (Annually Managed Expenditure)	95%	100%	Highly cashable. Short term percentage chosen to reflect potential ongoing administrative tasks when people return to work.
HM Revenue and Customs	100%	100%	Tax take assumed to be fully cashable
Schools	50%	75%	Most school savings relate to extra provision (e.g. for exclusion). Most of these costs are cashable in the longer term.
Housing Providers	80%	90%	Many of the costs relate to reduced evictions (legal costs, repairs, rent write off etc.) and are therefore relatively cashable.

6.2 The following table gives cashability values by outcome for the core outcomes included in the current version of the GM CBA model. The values have been derived by applying the agency cashability percentages detailed above to the benefits profile by agency, as given in the CBA model and accompanying guidance.[2]

Outcome	Short term / small scale cashability	Long term / large scale cashability
Reduced benefit payments – Job Seekers Allowance	91%	97%
Reduced benefit payments – Employment and Support Allowance / Incapacity Benefit	85%	94%
Reduced benefit payments – Lone Parent Income Support	90%	97%
Improved skills levels (to Level 2/3 qualifications)	100%	100%
Reduced adult mental health problems	22%	53%
Reduced unnecessary A&E attendances	20%	50%
Reduced incidents of domestic violence	25%	57%
Reduced incidents of anti-social behaviour (further action / no further action)	51%	78%
Reduced incidents of crime (all crimes)	24%	54%
Reduced housing evictions	75%	89%
Reduced statutory homelessness	49%	89%
Reduced incidents of taking children into care	50%	90%
Reduced drug dependency	22%	52%
Reduced alcohol dependency	20%	50%
Reduced persistent truancy (<85% attendance at school)	24%	54%
Reduced numbers of children excluded from school	47%	86%
Reduced hospital admissions	20%	50%
Reduced residential care admissions	50%	90%

[2] Supporting public service transformation: cost benefit analysis guidance for local partnerships (HM Treasury, 2014). Available at https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/300214/cost_benefit_analysis_guidance_for_local_partnerships.pdf